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FISCAL REVIEW COMMITTEE
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FISCAL REVIEW COMMITTEE STAFF REPORT

PROPOSED REQUEST FOR PROPOSAL FOR OPERATION OF SOUTH CENTRAL CORRECTIONAL FACILITY

DECEMBER 13, 2006

Introduction

The Fiscal Review Committee is required by law to review the draft request for proposal (RFP) for the new contract for operation of the South Central Correctional Facility (SCCF) in Wayne County. The Committee staff has conducted a background review and analysis consisting of the following:

- Review of the 2001 RFP and contract entered into with Corrections Corporation of America (CCA);
- Multiple meetings with officials of the Tennessee Department of Correction (TDOC) in Nashville;
- Review of prison operation and cost data provided by TDOC for SCCF, Northeastern Correctional Center (NECC) and Northwest Correctional Center (NWCC), the two prisons designated for comparison in reviewing performance and cost in operation of SCCF by CCA;
- Tour of SCCF and meetings with the warden, her staff, and corporate officials of CCA;
- Meeting with TDOC's contract monitors for SCCF;
- Tour of NECC and meetings with the warden and his staff;
- Review of the proposed 2006 RFP and pro forma contract;
- Meeting with staff of the Select Oversight Committee on Corrections; and

- Attendance at the Governor's budget hearing for TDOC.

Based upon this review, the FRC staff has prepared this overview and outline of issues for consideration by the Committee in evaluating the proposed RFP.

Overview

The prison privatization statute authorizes, but does not require, the State to contract for the operation of a facility by a private vendor. CCA operates SCCF pursuant to a five-year contract awarded in 2002. CCA has operated the prison continuously since 1992. The current contract expires on June 30, 2007. By law, CCA is required to operate the facility at a cost at least five percent less than the State's cost of operating comparable facilities (NECC and NWCC). The contract will cost the state approximately $25 million in FY06-07 (not including administrative and contract administration costs incurred by TDOC for SCCF).

CCA successfully completed a cost and performance comparison in 2004 after two years of experience with the contract. The comparison concluded that CCA had met the statutory requirement of cost savings of at least five percent below the state's comparable cost and had similarly met required performance standards. The FRC staff report dated May 3, 2005, documented savings by CCA of 11.1 percent (allowing a deduction from CCA's costs for sales and use taxes paid). Based upon that two-year review, the contract was extended to its full five-year term.

There are two mechanisms in the statute for increasing costs during the term of the contract. The first is an annual escalator during the contract term based upon the Consumer Price Index (CPI). This mechanism is not utilized in the current contract.

The second mechanism allows for price increases "if the general assembly specifically authorizes those adjustments and appropriates funds for that purpose, if required." Tenn. Code Ann. § 41-24-104(b)(2). This process is utilized in the current contract. It is described as a "contract inflator" and is included as an improvement each year in the Governor's budget.

Under the current contract, the annual contract inflator is 3.3 percent. This amount, which is greater than the CPI increase during the period 2002-date, was negotiated between CCA and TDOC.

During the term of the current contract, TDOC's cost of operating state prisons has increased substantially, largely as a result of wage and benefit increases provided to correctional officers and other prison staff. The cost increase for operation of state prisons has substantially exceeded the contract inflator in the current SCCF contract. Thus, the difference between the cost of operating the comparable state prisons and the cost of the state's contract with CCA has grown wider. The state has achieved greater savings in the past two years of the contract and will also achieve greater savings in the last year of the contract. In the final year of the contract, the State's total cost for SCCF (including administrative costs and the contract cost) will be approximately 15.7 percent less than the cost of the comparable state prisons.

Going forward, TDOC has proposed a contract inflator for FY07-08 of $4 million, which will cover the first year of the new contract. The inflator is approximately a 15.6 percent increase over the last year of the existing contract. TDOC's rationale for this increase is that it will keep the SCCF contract cost at approximately five percent below the state's cost of operating NECC and NWCC. This inflator is reflected in the maximum acceptable bid which TDOC proposes to specify in the RFP.

The existing cost differential may be reflected in prison operations, although this conclusion could not be definitively established based upon the information available to the FRC staff. It warrants further assessment (see Issues for Consideration section).

Currently, according to Warden Lindamood of SCCF, beginning correctional officers are paid $8.72 per hour. After six months, a new correctional officer receives a pay increase to $9.14 per hour. This wage compares with a beginning wage of $11.42 per hour for state correctional officers. In addition, the benefits offered to state correctional officers are substantially greater, particularly in the areas of insurance and retirement. The pay and benefits differential is such that Warden Lindamood and the TDOC contract monitors agreed that employees at SCCF would jump at the chance to work at the adjacent state prison facilities.

SCCF experiences high turnover in correctional officers. Warden Lindamood estimated the current annual turnover rate at 48-49 percent. Non-CCA officials estimated turnover at 75-80 percent. At the time of our visit to SCCF on November 17, 2006, FRC staff asked for data from SCCF to confirm the turnover statistics. CCA agreed to provide this information but to date it has not been received. The turnover rate at NECC and NWCC varies from 15 to 26 percent according to records of NECC and other data from TDOC.

SCCF, a combination medium- and minimum-security facility, also experiences a high rate of violent incidents as measured by TDOC. In FY05-06, SCCF had 7.43 violent incidents per 100 inmates, compared with 2.83 at NECC and 6.52 at NWCC. Although NECC and NWCC are not maximum-security institutions, NECC permanently houses some maximum security prisoners. The system-wide average, including maximum-security prisons, was 5.70.

CCA disputes these statistics. CCA contends that it over-reports violent incidents to err on the side of caution and that some violent incidents at the comparable state prisons are not reported.

Likewise, CCA contends that it has incurred sharp increases in costs for inmate health care in the past two years due to the changing health care status of inmates that it receives. In general, CCA contends that it is receiving a less healthy set of inmates and that its costs are being driven higher as a result. CCA contends that the $4,000 contractual cap on its in-patient health care costs is being overwhelmed by out-patient costs, which are not capped.

The infirmary and pharmacy facilities at SCCF and NECC appear to be similar. NECC has a physician and a dentist on duty 40 hours per week. SCCF has a physician on-site two days per week and utilizes a physician's assistant as well.

FRC staff did not attempt to resolve these conflicting assessments but believes that these and other issues warrant further consideration in the RFP process, as outlined below.

<u>Issues for Consideration</u>

1. Whether the RFP should require that the contractor meet the cost savings standard as determined by FRC.

Under prior law, for the contract to be extended for the final three years, the contractor had to meet the five percent cost savings standard for the first two years as determined by FRC staff based upon criteria set out in the RFP and the contract. (The contractor also had to meet performance standards.) Chapter 883 of the Public Acts of 2006 amended this statute to make the cost comparison a "consideration" but not the deciding factor in determining whether the five percent savings requirement had been achieved.

Although the comparison is no longer determinative under the statute, TDOC has authority to make it determinative under the terms of the RFP and the contract. The criteria for the cost comparison have not changed from the current contract in the proposed RFP, but the draft RFP makes the cost comparison only a consideration, not determinative, in making the five percent savings assessment. The Committee may want to consider whether to recommend modifying the RFP to make the FRC cost comparison determinative.

2. Whether TDOC should delete language from the RFP that would specify a maximum bid that TDOC will accept.

In an environment in which it is entirely possible, perhaps likely, that only one bid will be received, specifying a maximum bid that TDOC will accept is tantamount to inviting the bidder to bid at that amount. This strategy virtually ensures that the state will achieve savings no greater than five percent. If a maximum bid is not specified, a bidder is more likely to make its lowest and best bid. For this strategy to work, however, TDOC must be prepared to "walk away" from the process and operate the prison directly if no satisfactory bid is received.

The Committee may want to consider whether to recommend deleting the language from the RFP specifying a maximum acceptable bid.

3. Whether TDOC should modify the RFP process so that it can engage in further negotiations with a proposed vendor after receiving a response to the RFP.

TDOC should structure the contract award process so that the state's considerable leverage in negotiating for the operation of SCCF can be fully utilized. Again, this strategy requires a willingness by TDOC to walk away if negotiations do not produce an acceptable result.

The Committee may want to consider whether to recommend modifying the RFP process to increase the state's leverage in negotiations for the new contract.

4. Whether the RFP should be amended to strengthen the Comptroller's authority to audit the contractor to assess issues such as turnover, its effect on violent incidents in the prison, and the ability of the contractor to meet its obligation to provide safety and security comparable to a state prison.

The contractor has a fundamental obligation under the prison privatization law to provide safety, security, and constitutionally required services at the same level as a state prison. The level of staff turnover and the apparent rate of violent incidents at SCCF raise concerns about whether these requirements are being met. These concerns warrant a thorough review by the Comptroller, including review of employment and disciplinary records, to determine whether the cost savings achieved by the contractor through lower wages are having a negative impact on safety, security, or other basic prison functions.

The Committee may want to consider whether to recommend modifying the RFP to increase the Comptroller's authority to audit for these issues. The Committee may further want to consider requesting that the Comptroller make such an assessment and report to the Fiscal Review Committee and the Select Oversight Committee on Corrections on the results of the assessment.